BRIEF IN SUPPORT OF THE PETITION

Opinions Below

The opinion of the District Court appears on pages 154-168 of the record and is reported in 60 F. Supp. 37. The opinion of the Circuit Court of Appeals appears at pages 177-179 of the record and is reported in 153 F. (2d) 425.

Jurisdiction

The judgment of the Circuit Court of Appeals was entered February 6, 1946 (R. 180). Jurisdiction is conferred upon this Court by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925, C. 229 (43 Stat. 938).

Question Presented, Statutes Involved, etc.

A statement of the question presented, specifications of errors to be urged, and a statement of the case will be found in the petition. The statute involved is set forth in the Appendix, pp. 15-17, infra.

Argument

Section 204 of the Revenue Act of 1928 imposed an income tax on insurance companies other than life or mutual. The statute did not define the term "insurance companies other than life or mutual". However, in *Bowers* v. *Lawyers Mortgage Company*, 285 U. S. 182, supra, this Court adopted a test for determining what is an insurance company other than life or mutual, within the meaning of the Revenue Act. The Court said, at page 188:

> "While name, charter powers and subjection to state insurance laws have significance as to the busi-

> ness which a corporation is authorized and intends to carry on, the character of the business actually done in the tax years determines whether it was taxable as an insurance company."

Though the Court stated that the character of the business actually done determines whether a company is taxable as an insurance company, it did not specifically define the meaning of the term "character", or what elements determine the character of the business done. It found, however, that the premiums from guarantee for the years 1922 and 1923 amounted to about one-third of the company's total income, and concluded that "the element of guaranty involved in its transactions in the tax years was not sufficient to make it an insurance company."

On the same day the *Bowers* case was decided, this Court also decided the case of *United States* v. *Home Title Insurance Co.*, 285 U. S. 191, supra. In that case the Court found that Home Title Insurance Co. was taxable as an insurance company because its combined income from premiums for title insurance and mortgage guaranty and from charges for services incident to such insurance was the greater source of its income. This Court said, at page 195:

> "The amounts received as compensation for insuring titles, for guaranteeing that mortgages are first liens, and for guaranteeing payment, constitute the larger part of respondent's income. And, when there are added the fees and charges for examination of title, appraisals, and other services incident to its insurance business, the total properly assignable to that business amounts to more than 75 per cent of all respondent's income. Undeniably insurance is its principal business".

From these two decisions, it appears, therefore, that when this Court stated that whether a company was an insurance company or not was determined by the character of the business it did in the tax year, the Court had reference to the activities of the company producing its income—if

insurance was the principal source of its income, it was an insurance company and taxable as such.

The Circuit Court of Appeals in the case at bar reached the opposite conclusion. It stated (R. 178, 179), 153 F. (2d) 426:

> "* * *However, the test which determines the taxability of the corporation on the various items of income it received is not whether the term 'insurance company' aptly described the corporation itself because of the proportionate amount of its gross or net income received from activity properly classified as insurance. Instead, as shown by the Bowers case, *supra,* it is the character of the business it did to produce the particular income taxed. 8 Mertens, Law of Federal Income Taxation (1942) §§ 44.04, 44.05."

It thus appears that there is a conflict between the decisions of this Court in the *Bowers* and *Home Title* cases, supra, and the decision of the Circuit Court of Appeals in the instant case. This conclusion of the Circuit Court of Appeals is also in conflict with the decision of the Circuit Court of Appeals for the Third Circuit in the case of *National Commercial Title & Mortgage Guaranty Co.* v. *Duffy, et al.,* 132 F. (2d) 86. In approving the proportionate method of determining insurance company classification, the Court said:

> "The trial judge was therefore warranted in finding that the greater portion of the taxpayer's income was derived from non-insurance sources and in concluding that the plaintiff was not taxable as an insurance company during the years in controversy."

In applying the proportionate method of determining insurance company classification to the instant case, it will be found that there has been a substantial change in the character of the business transacted by the Company in the year 1931, as compared with the years 1922 and 1923. In 1922, the Company's income from premiums was $619,986.38 and in 1923, it was $750,803.21, about one-third of its total income in each of those years (285 U. S. 188, 190). By 1931,

its insurance business had grown so large that its premium income for that year was $2,051,721.67 (R. 143), almost three times as much as for 1922 and 1923. *This amount of $2,051,721.67 represented over 48% of its total income for 1931, of $4,267,343.55, constituting, by itself, the biggest source of income for that year.*

If, as this Court found, Home Title Insurance Co. was an insurance company because "insurance is its principal business" (285 U. S. 191, 195), then, by analogy, this Company was also an insurance company in 1931. The testimony in the instant case (R. 30-32) clearly discloses that the Company's practice in 1931 in the guaranteeing of first mortgage loans was to perform, and make almost the same charges for, the services shown in the *Home Title* case to have been rendered by that company in the conduct of its mortgage guarantee business. Thus, when, as in the *Home Title* case, there is added to the Company's premium income of $2,051,721.67 for 1931, its income of $1,054,801.02 from charges for inspections, appraisals and related services, which services this Court held in that case to be "incident to its insurance business", the total of the Company's income assignable to its insurance business in 1931 amounts to $3,106,522.69, or more than 72% of its total income for that year.

It is therefore apparent that the Company's principal business in 1931 was insurance and that it was subject to tax for that year as an insurance company under Section 204 of the Revenue Act of 1928.

Furthermore, the decision of the Circuit Court of Appeals is in conflict with the Treasury Regulations, Section 29.3797-7 of Regulations 111. That section, defining the term "insurance company" states as follows:

> "Though its name, charter powers, and subjection to State Insurance laws are significant in determining the business which a corporation is authorized and intends to carry on, the character of the business actually done in the taxable year determines whether it is taxable as an insurance company under the Internal Revenue Code. For example, dur-

> ing the year 1942 the M Corporation, incorporated under the insurance laws of the State of R, carried on the business of lending money in addition to guaranteeing the payment of principal and interest of mortgage loans. Of its total income for the year one-third was derived from its insurance business of guaranteeing the payment of principal and interest of mortgage loans and two-thirds was derived from its noninsurance business of lending money. The M Corporation is not an insurance company for the year 1942 within the meaning of the Code and these regulations".

The Treasury Department thus interprets this Court's decisions to mean that the term "the character of the business actually done in the taxable year" has reference to the activities of the company producing its income, and it is an insurance company if insurance is the principal source of its income. The Circuit Court of Appeals refers to this ruling in its opinion (R. 178) but in spite of that, holds that the proportion of income received by the Company from its insurance business in 1931 has no bearing upon the question whether it is an insurance company or not.

The above Treasury regulation is the same as Section 19.3797-7 of Reg. 103 (1940); Article 901-7 of Reg. 101 (1938); Art. 1001-7 of Reg. 94 (1936), as amended by T. D. 4759, 1937-2 C. B. 117. This regulation having been in effect without change for a number of years despite subsequent reenactment of Section 204 of the Code, it should have been given consideration by the Circuit Court of Appeals. In *Massachusetts Mutual Life Ins. Co.* v. *United States,* 288 U. S. 269, supra, this Court said, at page 273:

> "The Congress in the Revenue Acts of 1928 and 1932 reenacted Section 245 without alteration. This action was taken with knowledge of the construction placed upon the section by the official charged with its administration. If the legislative body had considered the Treasury interpretation erroneous, it would have amended the section. Its failure so to do requires the conclusion that the regulation was not inconsistent with the intent of the statute (citing cases)."

See also, *Brewster* v. *Gage*, 280 U. S. 327, supra; *Helvering* v. *R. J. Reynolds Tobacco Co.*, 306 U. S. 110, supra.

Similarly, since Congress did not define the term "insurance companies other than life or mutual", and this Court ruled that whether a company is taxable as an insurance company is determined by the character of the business actually done in the tax years, and the Treasury Department has interpreted the word "character" to mean the proportion that a company's income from insurance is to its total income from all sources, it is reasonable to assume that if this was contrary to the intent of Congress, the tax laws would have been revised to define an "insurance company" in such terms as to make the definition clear and unambiguous.

Conclusion

It is respectfully submitted that the decision of the Circuit Court of Appeals is erroneous. The question presented is of importance in the administration of the tax laws. The conclusion reached by the District Court and the Circuit Court of Appeals is apparently contrary to that reached by this Court in the *Bowers* case and the *Home Title* case. It is also in conflict with the decision of the Third Circuit in the *National Commercial Title* case, and is contrary to the regulations of the Treasury Department.

It is therefore respectfully submitted that the petition should be granted.

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